

California Real Estate Withholding Information for Sellers and Buyers

Who should read this information? If you are the buyer, an individual selling property, or a trustee of a revocable trust that holds title to the property being sold, you should read this information.

This information is not applicable if you are representing a seller that is a corporation, estate, irrevocable trust, limited liability company, or partnership. Get Form 593-W, *Real Estate Withholding Exemption Certificate and Waiver Request for Non-Individual Sellers*, for information on the withholding requirements when the seller is not an individual.

What is real estate withholding? Real estate withholding is a prepayment of California state income tax for sellers of California real property.

When is withholding required? Withholding is required on all transfers of real property by individuals unless:

- The property is being foreclosed upon, or
- The seller qualifies for one of the exemptions discussed in this brochure.

What is the withholding rate? The withholding rate is 3 1/3 percent of the total sales price. For example:

Total sales price	\$500,000
Withholding rate	<u>x 3.33%</u>
Withholding amount	\$ 16,650

Who must withhold? The law requires the buyer to withhold when the escrow person has properly notified the buyer of the withholding requirements. However, as part of the escrow services, the escrow officer generally assumes the responsibility for withholding or documenting why no withholding was done and for sending payment to the Franchise Tax Board. If the buyer has been notified of the withholding requirements, the buyer is liable for any penalty for failing to withhold.

What is the penalty for not withholding? The penalty for not withholding is the greater of \$500 or 10 percent of the required withholding amount.

What transactions are exempt from real estate withholding? Transactions are exempt from withholding if:

- The total sales price is less than \$100,000.
- The property qualifies as the seller's principal residence under Internal Revenue Code (IRC) Section 121. Generally, a home will qualify as a principal residence if, during the five-year period ending on the date of sale, the sellers owned and lived in the property as their main home for at least two years. There may be other restrictions, limitations, or exceptions for special circumstances. For more information, get IRS Publication 523, *Selling Your Home*, at www.irs.gov or contact the IRS toll free at (800) 829-3676.
- The seller will incur a loss on the sale for California income tax purposes. The seller must complete Form 593-L, *Real Estate Withholding-Computation of Gain or Loss*.
- The property is being involuntarily converted and will qualify for nonrecognition of gain for California income tax purposes under IRC Section 1033.

In addition, withholding may be reduced or deferred when:

- The sale qualifies as an IRC Section 1031 exchange. However, withholding will be required on any cash the seller receives.

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- The sale is an installment sale and the buyer agrees in writing to withhold on each principal payment including the down payment and any balloon payment. The buyer must complete Form 593-I, *Real Estate Withholding Installment Sale Agreement*.

Is withholding required if there is not enough cash? Yes. The parties must arrange to pay the withholding unless the seller qualifies for one of the exemptions listed above.

How can the seller claim an exemption? Sellers who qualify for an exemption should complete Form 593-C, *Real Estate Withholding Certificate for Individual Sellers*, and give it to their escrow officer within the first five days of opening escrow or as soon as possible to avoid delaying close of escrow. As with all tax documents, sellers are required to provide their social security numbers and sign under penalty of perjury that they meet the exemption. Form 593-C is available from escrow officers or on the FTB Website at www.ftb.ca.gov

What is the penalty when a seller falsely claims an exemption? The penalty is the greater of \$1,000 or 20 percent of the required withholding amount.

If the seller is withheld upon, how does the seller get the withholding back? When escrow closes, the escrow officer will give the seller a completed Form 597, Real Estate Withholding Tax Statement, showing the withholding. To claim the credit, the seller must, at the end of the year, file a California personal income tax return and attach the completed Form 597 to the front of the return. If withholding exceeds the seller's actual tax liability, the state will refund the overpayment. If the withholding is less than the actual tax liability, additional tax will be due.

Does my real estate agent have any responsibilities for withholding? No. Real estate agents have no responsibilities regarding withholding. If you want advice concerning real estate withholding and your specific tax situation, you should seek professional advice and counsel from an accountant, tax specialist, or an attorney.

Does my escrow officer have any responsibilities for withholding? Escrow officers are required to notify buyers in writing of the withholding requirements. Generally, the escrow officer will also assume responsibility for withholding as part of the escrow procedures. If you want advice concerning real estate withholding and your specific tax situation, you should seek professional advice and counsel from an accountant, tax specialist, or an attorney.

How do I get more information about real estate withholding? Visit the FTB Website at www.ftb.ca.gov to find answers to frequently asked questions, updates, Form 593-C, and also the Real Estate Withholding Guidelines (Pub. 1016). You may also contact the Withholding Services and Compliance Section at the Franchise Tax Board. See the contact information below.

Contact Information

Office Hours: 8:00 – 5:00, Monday through Friday
U.S. Toll-Free Call: (888) 792-4900
Local or International: (916) 845-4900
Tax Practitioner Hot Line: (916) 845-7315
TTY/TDD for hearing impaired: (800) 822-6268
Website: www.ftb.ca.gov

This information is only valid through December 31, 2003. For sales closing on or after January 1, 2004, please check our Website, www.ftb.ca.gov, for up-to-date information.

California Franchise Tax Board

September, 2003